

PEDCO ENERGY LIMITED

A Petroleum Exploration and Development Company

Suite 200, 301 Third Avenue S.W.
Calgary, Alberta T2P 2X9
Phone (403) 262-2720

Winspear Business Reference Room
University of Alberta
1-18 Business Building
Edmonton, Alberta T6G 2R6

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TO THE SHAREHOLDERS

Good News! Pedco Energy Limited is pleased to report it's financial and operating results for the year ended December 31, 1988. This year, oil revenues net of royalties increased from \$336,551 in 1987 to \$527,210 in 1988. This is also enhanced by additional investment income of \$115,715. In summary, the net earnings for the year is \$383,527 or 11.9¢/share.

OIL AND GAS ACTIVITIES

The Company continues to develop its Rose Creek Property in the Pembina Area of Alberta. Pedco drilled 16 successful oil wells in 1988. All but one of these wells are on stream and producing satisfactorily. Daily production exceeded 100 barrels of oil per day in 1988 with further increases projected for 1989, as additional wells are drilled.

OUTLOOK

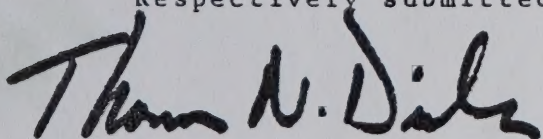
Pedco enters the 1989 fiscal year from a very positive base. The Corporation has continued to develop and increase it's substantial reserves in the Rose Creek Property by drilling to date an additional 7 relatively low cost "infill" wells.

Grant Trimble Engineering has completed a waterflood feasibility study. Their conclusion indicates that infill drilling along with a waterflood scheme is economically viable and should be implemented in 1990.

Pedco will continue to operate it's own drilling programs using the most cost effective methods available. The development of the Rose Creek asset continues to be enhanced by the use of Federal Government incentives and Alberta royalty free periods.

The oil business is now in a distinct upturn after many years of decline. The underlying fundamentals (i.e. consumption) are unmistakably improving. Hopefully OPEC should become increasingly more effective in administering oil prices. All of which bode well for increased earnings in Pedco for 1989 and beyond.

Respectively submitted on behalf of the Board.



Thomas N. Dirks
President
April 24, 1989

Fry & Associates

PEDCO ENERGY LIMITED

FINANCIAL STATEMENTS

To the Shareholders of
Pedco Energy Limited
FOR THE YEAR ENDED DECEMBER 31, 1988

We have examined the consolidated balance sheet of Pedco Energy Limited as at December 31, 1988 and the consolidated statements of earnings and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the corporation as at December 31, 1988 and the results of operations and changes in financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Alberta
March 15, 1989


Chartered Accountant



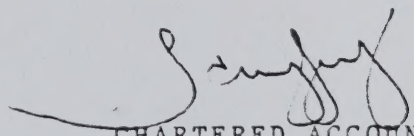
AUDITORS' REPORT

To the Shareholders of
Pedco Energy Limited

We have examined the consolidated balance sheet of Pedco Energy Limited as at December 31, 1988 and the consolidated statements of earnings and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures we considered necessary in the circumstances.

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Calgary, Alberta
March 26, 1989


CHARTERED ACCOUNTANT

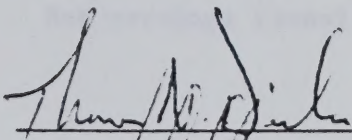
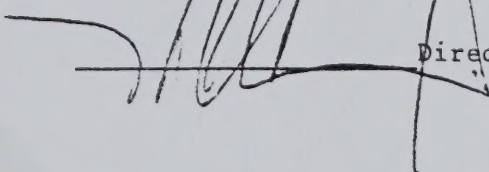
CONSOLIDATED BALANCE SHEET

	as at December 31	
	1988	1987
<u>ASSETS</u>		
CURRENT ASSETS		
Cash and term deposits	\$1,077,449	\$1,423,702
Accounts receivable (Note 5)	1,723,485	1,810,790
Other	77,082	-
	<u>2,878,016</u>	<u>3,234,492</u>
PETROLEUM AND NATURAL GAS PROPERTIES (Note 2)	<u>1,878,943</u>	<u>1,432,681</u>
	<u>\$4,756,959</u>	<u>\$4,667,173</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$2,855,023	\$3,187,914
SHAREHOLDERS' EQUITY		
Share capital (Note 3)	4,985,913	4,946,763
Deficit	(3,083,977)	(3,467,504)
	<u>1,901,936</u>	<u>1,479,259</u>
	<u>\$4,756,959</u>	<u>\$4,667,173</u>

APPROVED BY THE BOARD:

 Director
 Director

The accompanying notes are an integral part of these financial statements.

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CONSOLIDATED STATEMENT OF EARNINGS AND DEFICIT

	<u>Year ended December 31</u>	
	<u>1988</u>	<u>1987</u>
REVENUES		
Oil and gas revenue, net of royalties	\$ 527,210	\$ 336,551
Investment and other income	<u>115,715</u>	<u>32,889</u>
	<u>642,925</u>	<u>369,440</u>
EXPENSES		
Operating	71,646	74,036
General and administrative	32,647	84,514
Depletion and depreciation	130,105	54,996
Write-down of U.S. oil and natural gas properties	-	200,383
Write-down of investment	<u>25,000</u>	<u>-</u>
	<u>259,398</u>	<u>413,929</u>
EARNINGS (LOSS) FROM OPERATIONS	383,527	(44,489)
EXTRAORDINARY ITEMS		
Loss on disposal of investments	-	682,799
Mineral claims abandoned	<u>-</u>	<u>61,543</u>
NET EARNINGS (loss)	383,527	(788,831)
DEFICIT, beginning of year	<u>3,467,504</u>	<u>2,678,673</u>
DEFICIT, end of year	<u><u>\$3,083,977</u></u>	<u><u>\$3,467,504</u></u>
EARNINGS (LOSS) PER SHARE		
Earnings (loss) from operations	<u>11.9¢</u>	<u>(1.5¢)</u>
Net earnings (loss)	<u>11.9¢</u>	<u>(25.1¢)</u>

The accompanying notes are an integral part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	<u>Year ended December 31</u>	
	<u>1988</u>	<u>1987</u>
CASH PROVIDED BY (USED IN)		
OPERATIONS		
Earnings (loss) from operations	\$ 383,527	\$ (44,489)
Add items not affecting cash:		
Depletion and depreciation	130,105	54,996
Write-down of foreign oil and gas properties	-	200,383
Changes in non-cash working capital components	<u>(322,667)</u>	<u>890,705</u>
	190,965	1,101,595
FINANCING ACTIVITIES		
Proceeds on sale of properties	39,624	128,921
Issuance of common shares (Note 3)	<u>39,150</u>	<u>237,688</u>
	<u>269,739</u>	<u>1,468,204</u>
INVESTING ACTIVITY		
Purchases and exploration of properties	<u>(615,992)</u>	<u>(1,192,414)</u>
Net cash provided (used) in year	(346,253)	275,790
CASH AND TERM DEPOSITS, beginning of year	<u>1,423,702</u>	<u>1,147,912</u>
CASH AND TERM DEPOSITS, end of year	<u><u>\$1,077,449</u></u>	<u><u>\$1,423,702</u></u>

The accompanying notes are an integral part of these financial statements.



Fry & Associates
CHARTERED ACCOUNTANTS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 1988

1. SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation

These consolidated financial statements include the accounts of Pedco Energy Limited and its wholly-owned subsidiaries Laredo Petroleum Inc. and Aritex Resources Ltd.

Petroleum and natural gas properties

The Company is principally engaged in the exploration, development and production of oil and natural gas with all significant assets and operations located in Canada.

Substantially all of the Company's oil and gas activities are carried out jointly with others and these financial statements reflect only the Company's proportionate interest in such operations.

The Company follows the full cost method of accounting for oil and natural gas properties and related expenditures, whereby all costs related to the exploration for and development of oil and gas reserves are capitalized in country by country cost centres. Such costs include those related to lease acquisitions, geological and geophysical activities, lease rentals on non-producing properties and drilling of productive and non-productive wells. Proceeds from disposal of properties are normally deducted from the full cost pool without recognition of gain or loss.

Depletion and depreciation are provided using the unit-of-production method based upon estimated proven reserves, before royalties, converted to a common unit of measure using units of revenue.

The Company's petroleum and natural gas properties are subject to a ceiling test to ensure that the carrying value does not exceed estimated future net revenues from production of proven reserves valued at year-end prices less future administration, financing and income tax costs.

Other equipment

Other equipment is depreciated on a declining balance basis, over the estimated useful lives of the assets at rates varying from 20% to 30%.

Foreign currency translation

Accounts of foreign operations are translated into Canadian dollars using year-end rates of exchange for monetary assets and liabilities, historical rates of exchange for other assets and liabilities and average rates of exchange prevailing during the year for current income transaction. Gains or losses arising on foreign exchange translation are included in general and administrative expenses.

PEDCO ENERGY LIMITED

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 1988

2. PETROLEUM AND NATURAL GAS PROPERTIES

	<u>1988</u>	<u>1987</u>
Petroleum and natural gas properties	2,273,893	1,707,106
Office equipment	<u>58,720</u>	<u>47,462</u>
	2,332,613	1,754,568
Less: Accumulated depletion and depreciation	<u>(453,670)</u>	<u>(321,887)</u>
	<u>1,878,943</u>	<u>1,432,681</u>

3. SHARE CAPITAL

Issued:	<u>December 31, 1988</u>		<u>December 31, 1987</u>	
	<u>Number of Shares</u>	<u>Amount</u>	<u>Number of Shares</u>	<u>Amount</u>
Balance, beginning of year	3,143,236	\$4,946,763	2,850,069	\$4,709,075
Shares issued for cash				
Employee stock option exercised	15,000	7,650	92,000	69,000
Management fees paid with issuance of shares	70,000	31,500	72,000	54,000
Warrants exercised	<u>-</u>	<u>-</u>	<u>129,167</u>	<u>114,688</u>
Balance, end of year	<u>3,228,236</u>	<u>\$4,985,913</u>	<u>3,143,236</u>	<u>\$4,946,763</u>

As at December 31, 1988, 252,000 shares will be required to be reserved for issuance under the outstanding stock options at a price of \$0.45 per share. The options expire November 13, 1990.

Directors' options	145,000 shares
Employees' options	<u>107,000 shares</u>
	<u>252,000 shares</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 1988

4. INCOME TAXES

The Company has income tax loss carryforwards and drilling exploration and property costs totalling approximately \$3,264,000 available for deduction against future taxable income.

No provision has been made in the financial statements for any benefits arising from the utilization of the above income tax balances.

5. RELATED PARTY TRANSACTIONS

Amounts paid during the year to affiliated companies for management and related services totalled \$48,000 (1987-\$52,500). Amounts due from related parties as at December 31, 1988 were \$483,282 (1987-\$474,894). The company participates in various oil and gas exploration joint ventures with related companies.

